

BEFORE THE
POSTAL REGULATORY COMMISSION

Periodic Reporting
(Proposal Four)

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Docket No. RM2016-12

UNITED PARCEL SERVICE INC.'S REPLY COMMENTS TO THE
PUBLIC REPRESENTATIVE'S INITIAL COMMENTS
REGARDING PROPOSAL FOUR

(November 14, 2016)

United Parcel Service, Inc. (“UPS”) respectfully submits these Comments in reply to the Public Representative’s Initial Comments (“PR Comments”) in response to Proposal Four by the United States Postal Service (“Postal Service”), which proposes changes to the attribution of purchased highway transportation costs by revising the current assumption of 100% elasticity of purchased highway transportation capacity with respect to mail volume.

I. INTRODUCTION

While UPS agrees with a number of issues and recommendations raised by the Public Representative, there are a few points which deserve further comment and clarification. UPS’ economic experts, Dr. Kevin Neels and Dr. Nicholas Powers of The Brattle Group, in the report that accompanies these reply comments,¹ offer such clarification. UPS’ Initial Comments, the expert report filed along with those comments,² and the PR Comments make clear that the analysis underlying Proposal Four is fatally flawed. UPS respectfully asks the Commission to deny Proposal Four. UPS joins the Public Representative in asking the Commission to investigate the feasibility of constructing a dataset appropriate to study the variability of capacity with respect to volume in the future.

¹ Reply Report of Dr. Kevin Neels and Dr. Nicholas Powers To Accompany UPS Reply Comments in Docket No. RM2016-12, Dkt. No. RM2016-12 (November 14, 2016) (“Brattle Report”).

² Report of Dr. Kevin Neels and Dr. Nicholas Powers To Accompany UPS’s Comments in Docket No. RM2016-12, Dkt. No. RM2016-12 (Oct. 17, 2016) (“Initial Brattle Report”).

II. THE PROPER FOCUS OF THE COMMISSION IS ON LONG-RUN VARIABILITIES

First, UPS agrees with the Public Representative that a proper study of variability of capacity with respect to volume should focus on long term variability, while the Postal Service's model focuses only on short term variability.³ Volume-driven capacity adjustments in a large, complex system such as the Postal System often take the form of a reorganization of the system itself in order to continue to make efficient use of the system in the face of changing demands.⁴ For example, during the period studied by the Postal Service in the analysis underlying Proposal Four, the Postal Service was undertaking just such an extensive restructuring of its network in response to long term reductions in volume.⁵ Such reorganization takes time to bear fruit in the form of optimized capacity utilization, and the short time periods measuring variation in volume and capacity analyzed in Proposal Four cannot possibly take such reorganization and optimization into account.

A considerable portion of the variation of volume in the data underlying the Postal Service's analysis consists of routine day to day changes in mail volume. There are significant institutional, practical, and economic constraints preventing the Postal Service from optimizing its capacity every morning to fit that day's mail volume.⁶ Thus, even if the variability of capacity to volume is found to be significantly below 100% in studying day-to-day changes in volume and capacity, it is not this short-run variability

³ PR Comments at 4.

⁴ Brattle Report at 1-2.

⁵ Initial Brattle Report at 33.

⁶ Brattle Report at 3.

that should inform price attribution of purchased highway capacity. Focusing on short term variation of volume provides no insight into how capacity is adjusted in response to long term trends, and it is primarily these long term capacity decisions that drive the costs whose attribution Proposal Four seeks to modify.

The Postal Service has stated that the contracts it enters into with highway-transportation providers typically have a term of four years.⁷ Such contracts necessarily limit the ability of the Postal Service to optimize its capacity to match volume over the short term and suggest how long it would take for the Postal Service to adjust to a sudden and unforeseen change in mail volume.⁸ A study of capacity variability with respect to volume focused on durations shorter than the period it takes the Postal Service to actually adjust capacity will necessarily underestimate such variability. Low short term variability should not be baked into the attribution of what are essentially long term costs.

III. THE PRESENCE OF EXCESS CAPACITY IS FULLY CONSISTENT WITH A HIGH DEGREE OF VARIABILITY IN PURCHASED TRANSPORTATION COSTS

Second, UPS agrees with the Public Representative that a relatively stable level of excess capacity throughout the system over time is fully consistent with a variability of capacity with respect to volume close to 100%.⁹ As UPS noted in its Initial Comments, however, the capacity utilization measures in the TRACS dataset

⁷ See Postal Service response to question 2b of Chairman's Information Request No. 3.

⁸ Brattle Report at 3.

⁹ PR Comments at 24.

underlying Proposal Four cannot be used to measure the excess capacity along any given route in the Postal System, or the ability of that route to absorb growth in mail volume without expansion of capacity.¹⁰ The TRACS data takes the individual stop and route-leg as its unit of measurement. It is not designed for, nor is it capable of, depicting the volume and excess capacity along a route beyond that randomly sampled stop. As such, excess capacity as measured in the TRACS data is not meaningful when it comes to capacity decision-making. For example, the fact that a truck is 30% full at a given stop, without more information as to capacity utilization at other points on the route, is insufficient to inform such decision-making. It is also not informative as to whether and to what extent system-capacity changes are required in response to changes in system-volume.¹¹

IV. THE POSTAL SERVICE'S APPROACH TO MEASURING CAPACITY VARIABILITY IS FATALY FLAWED

The Public Representative attempts to salvage the analysis underlying Proposal Four by proposing various modifications.¹² As detailed in the Brattle Report, such an attempt is futile since the Postal Service's model cannot accurately measure the variability of capacity with respect to volume.¹³ No modification to the Postal Service's methods based on the TRACS dataset can successfully measure variability of capacity with respect to volume.¹⁴ The Public Representative's reintroduction of the zero-volume

¹⁰ UPS' Initial Comments at 4-7; Brattle Report at 4-5.

¹¹ *Id.* at 5-6.

¹² PR Comments at 9-16.

¹³ See Brattle Report at 7-11.

¹⁴ PR Comments at 7.

data into the analysis, for instance, only exacerbates the data and specification problems discussed in detail in UPS' Initial Comments.¹⁵

V. UPS JOINS THE PUBLIC REPRESENTATIVE IN RECOMMENDING THAT THE COMMISSION INVESTIGATE THE FEASIBILITY OF DEVELOPING A DATABASE APPROPRIATE FOR THE STUDY OF CAPACITY VARIABILITY

The Public Representative has provided a thorough discussion of the many conceptual and empirical inconsistencies between the accepted methodology for determining the variability of transportation costs with respect to capacity and Proposal Four's methodology for measuring variability of capacity with respect to volume.¹⁶ UPS agrees with the Public Representative that the analysis of each respective variability should be consistent and integrated. UPS supports the Public Representative's call for the Commission to investigate the feasibility of the Postal Service developing a database capable of supporting such an analysis of purchased highway transportation cost variability. Such a database would potentially be better-suited to the Commission's goal of improving the quality, accuracy, and completeness of the Postal Service's data, and would potentially allow for substantially more accurate attribution of costs to products.¹⁷

This docket has brought to light several inadequacies in the Postal Service's current data regarding capacity utilization. If the Commission undertakes to require a new dataset appropriate for the study of the issue in this docket, that dataset should, at

¹⁵ Brattle Report at 9-11; UPS Initial Comments at 7-8; Initial Brattle Report at 38-40.

¹⁶ PR Comments at 17-22.

¹⁷ Brattle Report at 11-13.

a minimum: (1) be informed by an understanding of the way capacity decisions are actually made and how those decisions are shaped by and reflected in the Postal Service's contracting protocols;¹⁸ (2) account for the amount of transportation that is actually provided and the ability of the Postal Service to vary capacity under existing contracts, as well as the cost of doing so;¹⁹ (3) cover all transportation provided over a continuous time period at a system-wide level, rather than measure only discreet randomly sampled stops, or trips, or days;²⁰ (4) use as its unit of observation at least the route, rather than individual stops or contracts.²¹

VI. CONCLUSION

Proposal Four does not remedy a significant inaccuracy nor does it significantly improve the quality, accuracy, or completeness of Postal Service data or the attribution of costs. The current assumption of 100% variability of capacity with respect to volume is reasonable and defensible. Proposal Four has failed to present reliable evidence to establish that the current assumption is incorrect, to establish alternative variabilities, or to demonstrate that the data that are currently collected by the Postal Service are capable of reliably doing so. The Commission should therefore reject Proposal Four.

¹⁸ *Id.* at 12.

¹⁹ *Id.*

²⁰ *Id.*

²¹ *Id.* at 12-13.

Respectfully submitted,

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